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Government rules 'smother' small businessman

By JERRY RUHL

News Staff

Government regulations are smothering the small businessman, according to Duane Pearsall.

After laboring for the past several months on a presidential committee, Pearsall is convinced that federal regulations force big business to become bigger.

"Regulations have caused industry concentration and raised the cost of market entry," Pearsall said.

"They have been adopted without regard for smaller companies," he said. "As a result, the costs of compliance, particularly the paperwork, has created a disproportionately heavy burden on smaller businesses."

Selected as National Small Business Person of the Year in 1976, Pearsall was named to the Domestic Policy Review Committee last fall. The Carter administration was seeking a 28-agency review of the role of government relative to industrial innovation.

The small business group of that committee prepared a supplemental report for the Department of Commerce and is currently preparing a booklet which summarizes its findings.

PEARSALL IS CURRENTLY working out of his home in Littleton as president of Small Business Development Corp., a vehicle for investing in small businesses.

He also serves as a consultant to the Statitrol division of Emerson Electric Co. Statitrol was founded by Pearsall in 1963 and introduced the first battery-powered smoke detector for home use. The firm was sold to Emerson in 1977.

"We will be trying to get this information to any member of Congress who will pick it up and run with it," Pearsall said last week.

"The regulatory process has spawned countless new social regulations over the past 10 years," Pearsall said. "Economist Murray Weidenbaum calculates that regulatory compliance will cost business almost \$100 billion in 1979 alone."

The subcommittee is not saying social regulations are wrong, according to Pearsall. He believes the two interests can be reconciled.

"The problem is that the regulations were not carefully constructed to give allowance for their impact on small business," he said.

"Small business hasn't had a strong voice in Washington and, inadvertently, has been victimized," Pearsall added.

A DRASTIC EXAMPLE is the effect of the Environmental Protection Agency on the cast metal industry, Pearsall said. "In the six years following the enactment of the 1968 EPA regulations, there were 350 verified foundry closings," he said.

"Approximately half of these closings were related to EPA requirements," he said.

Another example is in the battery industry, according to Pearsall.

Lead regulations set by the Occupational Safety and Health Administration resulted in a much larger per unit production cost for smaller plants, causing 113 single-plant battery firms to close and eliminating half the productive capacity not generated by the five major battery companies, Pearsall said.

"The result is that not only has the cost of entry to these industries become prohibitive, but large businesses, to maintain their source of supply for cast metal, have been forced to integrate vertically," he said.

Pearsall also cites studies which show that half of all significant new technology come out of small business. Yet the cost of research and development in small businesses was less than one-half the cost in large business, Pearsall said.

A SMALL BUSINESS which employs less than 200 people would pay 34 percent more per employee to hold a National Labor Relations Board election than a firm with more than 1000 employees, Pearsall said.

"Any paperwork or procedural activity has a harder cost impact on the smaller firm," Pearsall said.

Ray Kimball, president of the Colorado Association of Commerce and Industry, agrees with that conclusion.

Kimball said his organization performed a survey in Colorado two years ago which identified 184 government forms required for many businesses and 15 which were common to all types of business.

"We estimate that the average cost for a firm to fill out all this paperwork is \$745 per year for state forms and \$2,204 per year for federal forms," Kimball said.

"The volume of forms is simply more difficult for small firms to handle, as they lack the specialized staff," Kimball said.

Pearsall said there was no problem identifying examples of regulatory effects on small business when the subcommittee was exploring potential problems.

A mining company located on the West Coast told the group of five instances in which regulations had strangled its operations, Pearsall said.



Duane Pearsall

IN ONE INSTANCE the firm had developed a new method for mining uranium, Pearsall said. Due to the uncertainty of future water quality standards issued by the EPA, inability to secure financing forced it to sell out to a larger company, he said.

Later the same firm was involved in a joint venture which developed a contact lens which was 80 percent water and could be left in the eye for up to six months. The firm spent two years and \$250,000 to get approval from the Food and Drug Administration, Pearsall said.

Then the FDA issued new rules which would have required the firm to invest another \$250,000, he said. Frustrated, the small firm was forced to

over

sell the concept to a large corporation for further development, according to Pearsall.

Small companies often can't afford the cost of entry into new markets, Pearsall said.

He cited the Employee Retirement Income Security Act, passed in 1974, as drastically restricting the ability of small firms to raise capital from the public market.

Designed to prevent pension fund abuses, ERISA required pension fund managers to restrict investments to a "prudent man" standard, and stated they could be held personally liable for damages for deviations from this standard.

THE EFFECT WAS to exclude small firms from financing "through the largest single block of capital in the United States," according to Pearsall. "It forced every trust department in the country to stay out of small firm financing," he said.

Securities and Exchange Commission regulations also work against small businesses, according to Pearsall.

"Rule 146 of the SEC prevents investors from liquidating their investment in a small business," he said. "If a venture capitalist invests and the firm later goes public, it restricts how fast he can sell his stock."

In 1972, more than 600 companies went public, raising capital in excess of \$1 billion, according to Pearsall. By 1974, when ERISA went into effect, only four firms had public issues, Pearsall said.

In 1978 only 30 firms in the small business category filed a full registration to go public, Pearsall said.

There are all kinds of small firms which are ripe for going public but are forced to sell out to a big company because they can't raise capital," Pearsall said.

RECOMMENDATIONS OF the subcommittee focus on regulatory reform.

"Regulations should not specifically dictate the procedure of compliance, but should only outline performance standards," Pearsall said.

He would also like each regulatory agency to reduce the uncertainty of regulatory change by preparing a five-year plan. The plan would allow feedback from industry through advisory committees in a comprehensive review process.

"Regulations should be constructed with a consideration of three levels of business size with respect to compliance costs," Pearsall said.

Prior to initiating any new regulations, each agency should prepare an economic impact analysis, according to Pearsall.

He would also like to see tax incentives which allow small companies to attract venture capital. There should be a "flow-through of losses to investors within the year incurred."

"When small business cannot survive, big business must integrate vertically to support their own production needs," Pearsall said.